Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	McPherson	Analyst:	LuAnna Hass	Bill Number:	SB 677
Related Bills:	See Legislative History	Telephone:	845-7478	Introduced Date:	02-23-01
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Seismic Safety Requirement Costs Credit

SUMMARY

This bill would allow a credit for the certified final cost of seismic retrofitting necessary to comply with the California Building Standards Commission (CBSC) seismic retrofit building standards for hospitals.

PURPOSE OF THE BILL

The author's office has indicated that the bill's purpose is to offset a portion of the cost to retrofit hospitals required by state mandate.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective upon enactment. The bill would be operative for taxable years beginning on or after January 1, 2001.

POSITION

Pending.

ANALYSIS

<u>FEDERAL/STATE LAW</u>

Existing state and federal laws generally allow a depreciation deduction for the obsolescence or wear and tear of investment property or property used in a trade or business. The amount of this deduction is determined, in part, by the cost (or basis) of the property. In addition, the property must have a limited, useful life of more than one year. Depreciable property includes equipment, machinery, vehicles and buildings, but excludes land. Significant improvements to property generally extend the useful life of the property. The costs of significant improvements increase the basis of the property and are depreciated over the property's remaining useful life. Ordinary and necessary expenses to repair property used in a trade or business or held for the production of income that do not extend the useful life of such property are currently deductible.

Board Position:			Department Director	Date
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Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) or to influence behavior, including business practices and decisions (e.g., research credits or economic development area hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

THIS BILL

This bill would allow taxpayers a credit equal to an unspecified percentage of the certified final cost of seismic retrofitting paid or incurred during a taxable year to comply with the CBSC seismic retrofit building standards for hospitals as enacted in SB 1953 (Alquist, Stats. 1994, Ch. 740).

Any excess credit could be carried over indefinitely.

IMPLEMENTATION CONSIDERATIONS

The credit is limited to the certified final cost of seismic retrofit expenses, but provides no method to determine certified costs. The department does not have the expertise to verify whether a taxpayer's seismic retrofit construction meets the CSBC seismic retrofit standards and would therefore be eligible for the credit. The author may consider requiring the proper local authority to certify that the seismic retrofit meets the statutory requirements and requiring the taxpayer to obtain, retain, and provide evidence of this certification to the department upon request. The author may consider requiring the taxpayer to obtain this certification as a pre-condition to claiming the credit under this bill.

LEGISLATIVE HISTORY

AB 1118 (Corbett, 2001/02) would allow a credit equal to 55% of the amount paid or incurred for seismic retrofit construction on single-family or multiple-family residential structures constructed before 1979. This bill is in the Assembly Rules Committee.

SB 2051 (McPherson, 1999/00), a similar bill as introduced, would have allowed a similar credit for corporations. This bill failed passage in the Assembly Revenue and Taxation Committee.

AB 1756 (Scott, 1999/00) would have provided a credit equal to 55% of the amount paid or incurred for seismic retrofit construction on single-family or multiple-family residential structures constructed before 1979. This bill failed passage in the Assembly Appropriations Committee.

SB 875 (Marks, 1995/96) would have allowed a credit for an amount equal to 10% of the costs for rehabilitating a residential historic building and 20% for a commercial historic building. This bill failed passage in the Assembly Revenue and Taxation Committee.

SB 1628 (Marks, 1993/94) would have allowed a credit for an amount equal to 10% of the costs for rehabilitating historical buildings. This bill was held in the Senate Revenue and Taxation Committee.

PROGRAM BACKGROUND

Among other provisions of law, SB 1953 (Alquist, Stats. 1994, Ch. 740) required the CSBC to review, revise, and adopt seismic retrofit building standards for hospitals. Within three years after the adoption of the standards by the CSBC, all general acute care hospitals are required to develop a plan and schedule to bring the hospital into compliance with the standards. The hospital is required to be in compliance with the CSBC standards by January 1, 2030.

OTHER STATES' INFORMATION

A review of Oregon, Washington, and Alaska tax laws found no comparable credits relating to seismic safety. These states were reviewed because, like California, they have significant seismic activity.

FISCAL IMPACT

Once the implementation concerns are resolved, this bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Tax Revenue Estimate

The revenue impact for this bill would depend on the number of qualified buildings, the cost of retrofitting, and the amount of credits (credit percentage unspecified) that can be applied against available tax liabilities.

According to the Office of Statewide Health Planning, there are approximately 500 hospitals that would qualify for the credit provided under this bill. Out of those 500 hospitals, there are approximately 2,700 buildings that need to be retrofitted in order to meet the safety requirements. Approximately 850 of these buildings would not be retrofitted because of the cost to the hospital. These hospitals would change from an acute facility to a non-acute facility (outpatient). Out of the remaining 1,850 buildings, 850 were surveyed to be in good condition needing only non-structural repairs (i.e. lighting equipment), and the remaining 1,000 buildings would need both non-structural and structural retrofitting.

According to the Office of Statewide Health Planning and Seismic Safety Commission, individual hospitals have until 2002 to submit their plans to the Office of Statewide Planning for approval of seismic retrofitting construction. Some of the pre-1973 buildings have to be completed by 2008 and buildings constructed after 1973 have until 2030. It is unknown to what extent seismic retrofitting construction is needed for these buildings until the plans are submitted and approved. Based on a survey conducted by the Office of Statewide Health Planning, it was projected that the total cost for retrofits in 2008 will be approximately $10 billion and $14 billion for those completed in 2030, a total cost of $24 billion. Revenue losses would depend on the credit allowance percentage (as yet unspecified) and would not occur until after 2002.

ARGUMENTS/POLICY CONCERNS

In general, tax credits are provided to encourage taxpayers to incur certain expenses. This bill instead provides a credit for expenses that a taxpayer is already required to incur to comply with other laws.

Conflicting tax policies come into play whenever a credit is provided for an item that is already deductible as a business expense or is depreciable. This proposed credit would have the effect of providing a double benefit for taxpayers that are allowed to deduct the expense of seismic retrofit construction or include the seismic retrofit construction expense in their basis for depreciation. On the other hand, making an adjustment to reduce basis in order to eliminate the double benefit creates a difference between state and federal taxable income, which is contrary to the state's general conformity policy. In the case of a one-time business expense deduction, the reduction of that expense by the amount of the credit would not create an ongoing difference.

This bill does not specify a repeal date or limit the number of years for the carryover period. Credits typically are enacted with a repeal date to allow the Legislature to review their effectiveness. However, even if a repeal date were added, the department would be required to retain the credit on the tax forms indefinitely because an unlimited credit carryover period is allowed. Recent credits have been enacted with a carryover period limitation since experience shows credits are typically used within eight years of being earned.

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